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Financial and Disease Panics: Black Swans?

Some financial writers have claimed that stock market crashes such as followed the 2007 Bubble are unpredictable and rare. Calling them "Black Swan" events. More recently, the Covid-19 health threat has been described as a "Black Swan" event. Making the two together about as "Black Swanny" as it gets. However, a review of history suggests that severe financial crashes have always followed great financial bubbles. The transitions to busts have had much in common and the methodical pattern strongly suggests that even the greatest of crashes since the first in 1720 have predictable characteristics. Therefore, severe financial panics cannot be considered as "Black Swan" events.

And contagious diseases from epidemic to pandemic have been around for so long that while providing nasty periods may not be "Black Swan" events. What about now when the financial crash has been accompanied by a disease scare? It has happened before. In the mid-1500s Antwerp was the financial and commercial capital of the world. The brilliant trader, Thomas Gresham was the financial advisor to Elizabeth's government (*A Biography of Sir Thomas Gresham*). He assisted the Crown considerably during booms and busts. On one of the latter, Spain defaulted which was the power then.

That bust ran from 1560 to 1563 and Gresham wrote: "this plague time there is noe money nor credit to be had in the Streat of London". Meaning the Black Death accompanied a financial calamity. So, disease threats and crashes are nothing new.

Just how predictable was the current hit to the financial markets?

Since 1980, this writer has headed up a team that provides market research to fund managers. It has been based upon financial history and practical technical analysis.

In early October our research concluded that the stock and industrial commodity markets could enjoy strong rallies into "around January". We have called it the Turn-of-the Year trade and reviewed some outstanding examples. These included the mania in gold and silver that climaxed in January 1980, the wild Nikkei Bubble that completed at the end of 1989. Then there was the big bull market that drove the S&P to excesses in January 1973.
https://en.wikipedia.org/wiki/1973%E2%80%9374_stock_market_crash

All were followed by severe bear markets.

So it was important to recognize the top as it was happening and for this there are some questions, which were reviewed in our weekly publication of January 9th.

"Is the stock market up when it should be?" The answer was ***"Yes"***.

The next question was ***"Are there signs of speculation?"*** The answer included that our technical indicators had reached "Upside Exhaustions", which relates to momentum. Another indicator provided a "Sequential Sell" which relates to a trading pattern. Other

comments included that the stock market was very highly valued relative to GDP and the average wage. All of these determinants worked at previous cyclical peaks such as in 2007 and in 2000, the Dot-Com Bubble.

The high for the NYSE Comp was set on January 17th and the decline amounts to 19 percent.

Beyond these technical measures, warning events included that the Yield Curve inverted in the summer whereby short rates trade higher than long rates. This is typical of the culmination of any boom and the record back to 1857 is that every inversion has been followed by a recession. Beyond this, the curve inverted again in January. The double inversion occurred in 2007 as well as in the 1929 and 1873 Bubbles.
https://en.wikipedia.org/wiki/Panic_of_1873

Credit spreads which is the difference between high-grade and low-grade bonds have reversed to widening. Which also signals the end of the boom.

It is worth noting that while most think that Fed can keep a boom going by cleverly timed cuts to the Fed rate, there is no example of success. Success would be a record of no recessions. And the concept is ironical. Treasury Bill rates increase in a boom and record the fastest declines during a financial crisis.

Back in the early 1900s, policymakers knew that recessions followed setbacks in the credit markets. And the theory has been that with the Fed as "lender of last resort" financial crises would be eliminated, thus preventing recessions. There has been 18 recession since the Fed opened its doors in January 1914.
https://www.nber.org/cycles.html

More than a hundred years of evidence says that the theory, although very appealing, doesn't work.

Another feature of the transition from boom to contraction includes the action in industrial commodities. Up in the boom and down in the bust. Base metals set their recent high on January 16th and have declined by 12 percent. Crude became overbought in setting the high at $65.65 on January 8th and has crashed 50 percent to $32. Our February 13th publication noted our targets of $37 and $26.

These plunges are marking the transition to contraction and going the other way gold's price reverses to increasing in the post-bubble world. From the low of $1167 in 2018, gold has rallied 46 percent to $1702. Also Treasury Bills decline. For the 3-month the high yield was 2.49% a year ago in March. Now it is at 0.29%.

It's been called the "Everything Bubble" and our work notes that it has had much in common with the 1929 and 1873 examples. https://www.amazon.com/Everything-Bubble-Endgame-Central-Policy-ebook/dp/B0794RLM8R Clearly this has been the "Everything Correction" which importance is confirmed by an observation from the October 4, 1873 edition of *The Economist.* Although a month early in that Crash it was profound: ***"The panic may be over, but the results of the panic are not over."***

That post-bubble contraction completed in 1895.

Central bankers have been insisting that nothing can go wrong. Market history records that great financial bubbles have always been followed by lengthy contractions and recent developments have been on the methodical path to contraction.

One can never know ahead of time the reason the media will find to explain a significant financial setback. This one is marked by the astounding panic by China's Communist government in an attempt to maintain the myth of omniscience and omnipotence.

Dutch merchants in the 1700s noted that "easy" credit was associated with a boom. And the term in a contraction was "diseased" credit (*De Koopman*, December 1772).

While this historian does not see any financial "Black Swans", the Chicom deliberate panic seems a shatteringly fast "Grey" one.

Beyond this, the reality of a severe contraction could eclipse the promotion of Climate Hysteria.